traffic termination, the net revenue flow will be near zero. This leads to the conclusion that bill and keep arrangements may be relatively cost-based.

CPI endorses the solution that several states have adopted, to require bill and keep arrangements for a period of time in order to facilitate the early introduction of competition. We agree with the Commission's tentative conclusion that the Commission or the States may impose bill and keep arrangements as part of regulations and in arbitration. If local traffic termination measuring methods improve, it may be slightly more efficient, assuming measuring costs are small, to require the carriers to bill each other for the costs of termination. However, we think that bill and keep arrangements have numerous advantages which recommend their use.

VI. Resale

In addition to entering local markets by purchasing unbundled network elements, some local exchange competitors will likely purchase finished LEC services and resell them. The Telecommunications Act of 1996 places this duty on all LECs:

> (1) Resale.--The duty not to prohibit, and not to impose unreasonable or discriminatory conditions or limitations on, the resale of its telecommunications services.

Further, the Act imposes this additional duty on incumbent LECs:

> (4) Resale.--The duty
>
> (A) to offer for resale at wholesale rates any telecommunications service that the carrier provides at retail to subscribers who are not telecommunications carriers; and
> (B) not to prohibit, and not to impose unreasonable or discriminatory conditions or limitations on, the resale of such telecommunications service, except that a State commission may, consistent with regulations prescribed by the

> Commission under this section, prohibit a reseller that obtains at wholesale rates a telecommunications service that is available only to a category of subscribers from offering such service to a different category of subscribers.

Finally, the Act establishes the following pricing standard for resale:

> (3) Wholesale Prices for Telecommunications Services.--For the purposes of section 251(c)(4), a State commission shall determine wholesale rates on the basis of retail rates charged to subscribers for the telecommunications service requested, excluding the portion thereof attributable to any marketing, billing collection and other costs that will be avoided by the local exchange carrier.

As the Commission knows well, resale of long distance service is the method by which the vast majority of interexchange carriers have entered the long distance market. We expect that local exchange service will experience a similar influx of carriers (both large and small) willing to make their way on the difference between wholesale and retail prices for the services. We will comment on several issues concerning local resale raised by the Commission in its Notice.

First, we agree with the Commission's tentative conclusion in ¶175 that the range of restrictions which incumbent LECs may place on resale should be quite narrow. In particular, the LEC should be required to offer for resale any service which it offers for retail. This requirement should extend to all services, regardless of whether the LEC claims these services are priced at, above, or below cost. Since the price paid to the LEC for the resold service is retail price minus avoided cost, there is no logic in the argument that services priced "below cost" should not be resold. To begin with, the expression "below cost" probably means "below embedded cost" and does not refer to economic cost. Next, to the extent that the service receives a subsidy from a state or federal universal service fund, the underlying carrier receives the subsidy.

The wholesale price for a resold service should be based on the retail price, including any discounts or promotions. Any such discounts should be passed through to the reseller.

The Commission should permit States to determine the extent to which "arbitrage" between products is permitted through resale. The language in §251(c)(4) suggests that a State may restrict the resale of a service to the class of customers served by the LEC for the service. The reasonableness of such restrictions obviously will vary from state to state and is best determined by regulators in each state. We would expect some states to prohibit, for example, the resale of residential service to business customers. As long as the Commission and the States are careful to determine a fair "avoided cost" discount so that a reseller can reasonably be expected to compete, a restriction such as this is not unreasonable.

In ¶175 the Commission seeks comment on whether a LEC should be allowed to avoid the requirement of resale of a service by withdrawing the service from retail sale. We agree with the suggestion that a LEC, especially an incumbent LEC, has the ability to frustrate the development of competition by withdrawing services which another carrier wishes to resell. The recent decision by US WEST to withdraw its Centrex offering is claimed by resellers to have a serious anti-competitive effect and is being challenged in several states. On the other hand, we should expect a competitive market to result in many trials, false starts and failures by LECs, such that we would not want to unreasonably restrict their ability to offer (or withdraw) services relatively quickly. We suggest that the Commission's final rule on this issue identify service withdrawal as a potentially anti-competitive activity and leave it to State commissions to determine whether such has occurred. The rule should also require that the LEC accomplish any withdrawal in a manner that is competitively neutral. A LEC can mitigate (or be ordered to mitigate) the effect of the withdrawal of a product by such methods as grandfathering existing wholesale customers or by replacing the offering with a similar offering.

The Commission suggests that, in some cases, the availability of unbundled network elements may provide a substitute. However, the Commission should recognize that unbundled elements and finished product resale are two distinctly different methods for entering the local exchange market. Moreover, the business realities of a reseller may make it impossible to switch service offerings smoothly while trying to maintain quality of service to customers. In short, the existence of unbundled network elements should not be presumed to be a real substitute for a resold service, even if it is a theoretic substitute.

VII. Conclusion

The Competition Policy Institute appreciates the opportunity to comment on the Commission's Interconnection Rule. We commend the Commission for its pro-competitive orientation in the Notice and recommend that the final rule incorporate the suggestions made in these Comments.

Respectfully Submitted,

Ronald J. Binz
President

Debra Berlyn
Executive Director

Competition Policy Institute
1156 15th Street, N.W. Suite 310
Washington, D.C. 20005
202-835-0202 202-835-1132 (fax)